



Japan Post: Retreat or Advance?

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Legislation to reform Japan Post is again gathering steam in Tokyo. The real question is whether the latest act in this long-running drama will represent true reform or in fact will camouflage an entrenchment of Japan Post's formidable monopoly powers. Antireform proposals being lined up for consideration in the Diet would indefinitely extend effective government control of Japan Post's financial arms (thereby reversing the Koizumi era reforms). On the other hand, reform forces in the Japanese government want new legislation to guarantee a level playing field in banking and insurance between Japan Post and private firms, whether domestic or foreign. How the contest

between antireform and proreform forces plays out matters both to Japan and the world:

- Japan Post ranks among the largest state-owned enterprises (SOEs) on the planet, combining the world's largest bank and insurance operations with postal delivery under an umbrella holding company. If Japan Post cannot be made to operate on a level playing field with private firms, who can?
- Japan Post channels 80 percent of the financial savings of its Japanese account holders into Japanese government bonds, thereby ensuring gross distortion of Japan's internal capital market.
- Japan Post draws on a number of government privileges—most notably light regulation and exemptions from statutory prohibitions on strategic combinations—to market its own insurance products in competition with private insurance firms, both domestic and foreign-owned. At the same time, it has been unwilling to offer private insurance products other than through a small number of outlets in its vast postal distribution network.

The favorable treatment received by Japan Post from the government effectively tilts the playing field against foreign and domestic private banks and insurance firms. This is protectionism, pure and simple, and puts the government of Japan in clear violation of its commitments to the World Trade Organization (WTO). The Japanese government did not take an exemption for Japan Post when it signed the General Agreement on Trade in Services (GATS) in 1994; hence the operations of Japan Post and its financial units are inconsistent with Japan's international commitments under GATS Article XVII, National Treatment. Japan Post's operations are not

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only inconsistent with agreed international rules but also are bad for Japanese taxpayers and consumers. Taxpayers, whether they know it or not, are the ultimate guarantors of Japan Post's

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huge financial liabilities arising from its banking and insurance operations. Consumers miss the array of banking and insurance products that would be available if Japan Post did not occupy a privileged perch that crowds out private firms.

KOIZUMI REFORMS

In our Policy Brief in October 2010, *Turning Back the Clock: Japan's Misguided Postal Law Is Back on the Table*,¹ we recounted the recent history of reform efforts. The starting point was Prime Minister Junichiro Koizumi's landmark reform bill, passed in 2005, which envisaged substantial privatization by 2017. By October 2007, the state-run postal service was split into four companies under the umbrella of Japan Post Holdings Co. Ltd. The new companies were Japan Post Service, Japan Post Network, Japan Post Bank, and Japan Post Insurance. Koizumi's Postal Privatization Law scheduled 100 percent privatization of Japan Post Holdings' two financial subsidiaries by 2017.

TURNING BACK THE CLOCK

After the Democratic Party of Japan (DPJ) came to power in 2009, DPJ kingmaker and General Secretary Ichiro Ozawa, together with Shizuka Kamei, then minister of state for financial services and postal reform, sought to reverse the Koizumi reforms. On May 31, 2010, with almost no debate, the Lower House approved legislation that would restructure Japan Post Holdings and allow the government to hold one-third of its shares indefinitely, essentially a controlling position. Japan Post Holdings, Japan Post Service, and Japan Post Network would be merged into a single holding company, while Japan

1. Gary Hufbauer and Julia Muir, *Turning Back the Clock: Japan's Misguided Postal Law Is Back on the Table*, Policy Briefs in International Economics 10-17, October 2010, Peterson Institute for International Economics, www.piie.com.

Post Bank and Japan Post Insurance would be subsidiaries of the newly merged parent company, with at least one-third of their shares held indefinitely by the holding company. As a practical matter, the holder of one-third of the shares in the postal businesses will be able to exert control over them, particularly given the fact that the government is the shareholder and that the other shares are likely to be widely dispersed and/or held by institutions that can be expected to support the government's positions. Accordingly, if enacted into law, the Lower House bill would ensure that the government retained control not only over Japan Post Holdings but also over the two financial subsidiaries. At the same time, the procedural safeguards on insurance offerings of Japan Post Insurance would be largely removed.

The antireform bill ran aground during the second half of 2010. DPJ Prime Minister Yukio Hatoyama suddenly resigned on June 2, 2010 and was succeeded by Naoto Kan. Unlike Hatoyama, Kan was not an enthusiast for rolling back the Koizumi reforms, and he postponed consideration of the new legislation by the Upper House until the 2011 Diet session. Over the next year, intensive consultations were held between the DPJ, its coalition partner the People's New Party (PNP), the opposition Liberal Democratic Party (LDP), and the opposition New Komeito Party (NKP). The one solid outcome of these consultations was the death of the antireform bill passed by the Lower House in May 2010. It simply could not attract enough votes to pass the Upper House or win a "supermajority" (more than two-thirds of votes) in the Lower House.

POSTAL REFORM MEETS RECONSTRUCTION FUNDING

On March 11, 2011, the Great East Japan Earthquake (as it is called in Japan) struck the Tohoku area (Richter scale 9.0), unleashing a tsunami with a maximum height of 40.5 meters (unprecedented for a thousand years), leading to a calamitous meltdown of the Fukushima I Nuclear Power Plant. The loss of life from flooding (not radiation) was enormous—some 20,000 people—and 125,000 buildings were damaged or destroyed along with roadways, rail lines, and other infrastructure. The World Bank estimated direct and indirect economic losses at \$235 billion, the most expensive natural disaster on record. Numerous private relief efforts were quickly launched and the government announced its own relief plan costing ¥23 trillion or more (more than \$300 billion) during the ten-year reconstruction period.

The earthquake and its aftermath triggered devastating criticism of Tokyo Electric Power and the Japanese officials

responsible for nuclear oversight and disaster relief. As a direct consequence, on August 30, 2011, Prime Minister Kan resigned and was succeeded by his finance minister, Yoshihiko Noda.

Augmenting relief plans already in motion, Prime Minister Noda and his cabinet announced their basic policy in the Third Supplementary Budget and Reconstruction Funding, released on October 7, 2011. The Third Supplementary Budget was submitted by the Noda cabinet to the Diet on October 21, 2011, and included ¥12 trillion (\$156 billion) funding for reconstruction, almost all of which will be financed by the government issue of “reconstruction” bonds.

In its October 7, 2011 cabinet decision, the government planned to raise ¥7 trillion (almost \$90 billion) from “nontax revenue” over the next ten years to help finance the reconstruction bonds. Potential sources of nontax revenue included the sale of government shares in Japan Tobacco and Japan Post. Very quickly antireform forces within the government—notably the People’s New Party, a member of the DPJ ruling coalition—saw future sales of Japan Post shares as a vehicle for pushing their latest version of “postal reform” legislation. Japan Post would be “privatized” through the sale of up to two-thirds of government shares, but the government would retain at least one-third, effectively maintaining its controlling position. Nobody knows how much revenue the government can actually generate by selling shares in the Japan Post group, and the government’s retention of a controlling interest would clearly cut into the revenue objective. But aside from the revenue angle there is the all-important question of Japan Post’s business model in the decade ahead.

A new idea has emerged over the last few weeks from discussions between the ruling and opposition parties: “amendments” can be made, not to the moribund May 2010 legislation but rather to the existing Postal Privatization Law dating from the Koizumi era. The New Komeito Party floated a proposal to amend the existing law in a way that would merge two of the postal companies—Japan Post Service and Japan Post Network—into one firm and allow Japan Post Holdings to retain more than one-third of its shares in Japan Post Insurance and Japan Post Bank indefinitely. Just like the May 2010 bill, these “amendments” would effectively ensure that no member of the Japan Post group would leave the ranks of state-controlled enterprise.

On December 21, 2011, PNP President Shizuka Kamei (previously a minister of state for financial services and postal reform) and DPJ Secretary-General Azuma Koshiishi agreed to use NPK’s proposal as a basis to achieve early passage of the postal bill during the next Diet session. Their meeting was to be followed by intense DPJ consultations with opposition parties. However, the DPJ ended the year 2011 with

acrimonious in-party debate over a consumption tax hike and nine DPJ members left the party in opposition to the hike. Although the DPJ finalized its tax proposal on December 30, 2011, the outcome triggered harsh criticism from the opposition parties, including the LDP and NPK, which in turn rejected negotiations with the DPJ over the postal reform plan. Consequently Prime Minister Noda announced his decision to reshuffle his cabinet, which will likely take place January 13. Nevertheless, before or even during the upcoming Diet session, which will probably open around January 24, 2012, a new postal bill could be taking shape, in the form of amendments to the existing Postal Privatization Law—all put forward under the larger banner of reconstruction finance and the government’s efforts to minimize consumption tax hikes. In public pronouncements, the contradiction between the revenue goal and government retention of a controlling interest (through one-third share ownership) will be conveniently ignored.

POSTAL REFORM MEETS THE TRANS-PACIFIC PARTNERSHIP

Japan’s commitment to national treatment for foreign insurance firms and banks, extended to all WTO members in the 1994 General Agreement on Trade in Services, has long been contradicted by the practices of Japan Post.² After Prime Minister Noda’s declaration at the November 2011 Honolulu Summit of the Asia-Pacific Economic Cooperation (APEC) forum, throwing Japan’s hat into the Trans-Pacific Partnership (TPP) ring, the contradiction between commitment and practice has now reached the front burner. Japan Post’s operations not only violate the GATS but also are at odds with the SOE drafts now being circulated among the nine current TPP parties and four aspirants.³ While the draft SOE texts have not been released, certain principles seem highly likely:

- SOEs will be defined as state-controlled firms that engage in commercial transactions in competition with private firms.
- SOEs should buy and sell for commercial consideration.
- SOEs should be transparent with respect to their shareholders and organization.

2. The contradictions are explained in Hufbauer and Muir, *Turning Back the Clock*.

3. The nine current TPP parties are Australia, Brunei, Chile, Malaysia, New Zealand, Peru, Singapore, Vietnam, and the United States. The four aspirants are Canada, Japan, Korea, and Mexico.

- The national regulator should be nondiscriminatory as between SOEs and private firms.
- The national treatment principle must be respected.

Details of the new postal bill remain to be decided. However, the New Komeito-Kamei-Koshiishi outline is squarely “antireform” and if passed into law would create a major hurdle to Japan’s membership in the TPP. But it is possible that a constructive approach will be hammered out in consultations between the DPJ and opposition parties. Here

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we offer recommendations as to the tenor of a true Japan Post reform bill, one that would represent a step forward rather than a step back.

Ironically, privatization need not be the central goal, even if privatization was sufficiently bold that no member of the Japan Post group could be considered a state-controlled enterprise (SCE). The reason is that privatization per se will not ensure that the giant members of the Japan Post group dealt fairly with private firms. Nor will it ensure even-handed oversight by regulatory bodies.

Privatization should be part of postal reform legislation, both to raise reconstruction funds and to reinforce the transition to nonprivileged status for members of the Japan Post group. However, other elements are equally important:

- Japan Post Bank and Japan Post Insurance should not be permitted to extend their product offerings unless it is crystal clear that they no longer enjoy government privileges, including less stringent regulation than their private-sector competitors.
- To the extent that Japan Post Network distributes Japan Post Bank and Japan Post Insurance products through its vast network of postal offices, it should equally distribute the products of sound private bank and insurance firms.
- Japan Post Bank and Japan Post Insurance should be subject to the same licensing and holding company regulations as private firms under Japanese Insurance Business and Banking Laws. The Japan Financial Services Agency should treat Japan Post group members the same as private firms.
- Japan Post should pay all taxes under the same rules that apply to private firms, and they should publish statements audited under international accounting standards. Bank accounts and insurance policies that enjoy a government guarantee should be separately reported, and earnings from these products should not be used to cross-subsidize other accounts and policies.

It is critical for the postal reform bill to anticipate Japan’s membership in the TPP. This can be done by embracing the reforms just noted and reflecting the principles of draft SOE texts. As it evaluates Japan’s membership in the TPP, the US Congress will focus on three issues: autos, beef, and Japan Post. Rather than enacting postal reform legislation with a “step back” flavor—thereby creating a major hurdle to TPP accession—the Diet should seize this opportunity to enact postal reform that will be a true “step forward.”